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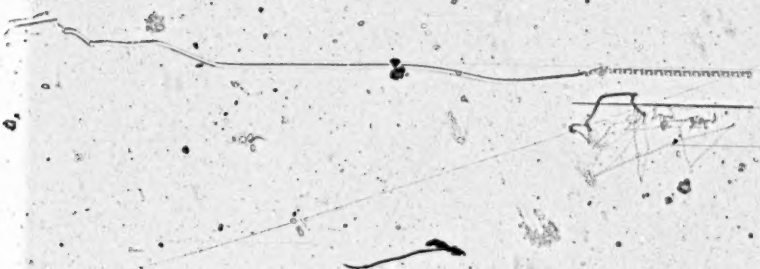
UNITED STATES, APPELLANT

v.

NEW YORK, NEW HAVEN & HARTFORD RAILROAD COMPANY

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF CONNECTICUT

BRIEF FOR THE UNITED STATES



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In the Supreme Court of the United States

OCTOBER TERM, 1951

No. 250

UNITED STATES, APPELLANT

v.

NEW WRINKLE, INC., AND THE KAY & ESS COMPANY

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF OHIO

BRIEF FOR THE UNITED STATES

OPINION BELOW

The district court did not render an opinion.

JURISDICTION

The judgments dismissing the complaint were entered on June 5, 1951 (R. 27–28). The petition for appeal was filed and allowed on July 24, 1951 (R. 28–29). The jurisdiction of this Court is invoked under Section 2 of the Expediting Act of February 11, 1903, 32 Stat. 823, 15 U. S. C. 29, as amended by Section 17 of the Act of June 25, 1948, 62 Stat. 869. On October 8, 1951, this Court noted probable jurisdiction of the appeal (R. 31).

QUESTIONS PRESENTED

1. Whether the allegations of the complaint that appellees conspired to fix uniform minimum prices and to eliminate competition throughout the wrinkle finish industry, by means of patent license agreements, charge a violation of Section 1 of the Sherman Act.

2. Whether a patentee who does not make or sell a patented product goes beyond his patent monopoly, and hence stands in violation of the Sherman Act, when he enters into substantially identical patent licenses fixing uniform minimum prices for some 200 licensees.

3. Whether two patentees act outside their patent monopoly and violate the Sherman Act when they unite their patents for the purpose of fixing prices, by creating a corporation to take over their patents and to grant price-fixing licenses thereunder.

4. Whether the prohibitions of Section 1 of the Sherman Act apply to a corporation which is a party to a conspiracy to restrain interstate commerce but does not itself engage in the commerce subjected to restraint.

STATUTE INVOLVED

Section 1 of the Act of July 2, 1890, 26 Stat. 209, known as the Sherman Act, as amended by the Act of August 17, 1937, 50 Stat. 693, provides in part:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal * * *. [15 U. S. C. 1.]

STATEMENT

This is a civil proceeding brought by the United States under Section 4 of the Sherman Act charging the defendants, New Wrinkle, Inc., and The Kay & Ess Company, with violating Section 1 of the Act. Shortly after the filing of the complaint in September 1948 (R. 1), the defendants (referred to herein as New Wrinkle and K&S) filed motions to dismiss (R. 23-26). The K&S motion asked for dismissal upon the ground that the complaint failed to state a cause of action. The ground of the New Wrinkle motion was that, since the complaint averred that New Wrinkle has at no time "engaged in the commercial manufacture and sale of wrinkle finishes", it has not engaged in interstate commerce and therefore "could not be" guilty of violating the Sherman Act. On June 5, 1951, the district court, without rendering an opinion, entered judgments dismissing the complaint, and recited in each judgment that the defendant's motion to dismiss is "well taken" (R. 27, 28). The Government appealed from these final judgments of dismissal.

The complaint alleges, and the motions to dismiss admit, the following:

For many years the defendants and those named in the complaint as co-conspirators have been engaged in a conspiracy in restraint of interstate and foreign commerce in wrinkle finishes, in violation of Section 1 of the Sherman Act (par. 13,[1] R. 3). The conspiracy has had the effect, "as intended by the defendants and co-conspirators," of fixing identical and unreasonably high minimum prices, discounts, and selling terms and conditions "for substantially all wrinkle finishes manufactured and sold in the United States," and of eliminating competition between the defendants and their co-conspirators in the sale of such finishes (par. 23, R. 5).

Wrinkle finishes are enamels, varnishes and paints which produce a hard wrinkled surface when applied to metal or other material. They have important advantages over ordinary enamels and varnishes and are widely used as surface coverings for typewriters, cash registers and many other articles. Approximately 1,000,000 gallons are sold per year and manufacturers receive from the sale of these products over $2,000,000 annually. The licensees of New Wrinkle manufacture "substantially all" of the wrinkle finishes produced in the United States, and a

[1] Our paragraph references are to paragraphs of the Government's complaint.

substantial portion of the wrinkle finishes which they make is sold and shipped to purchasers in states other than the state of manufacture, and to purchasers in Canada. (Pars. 8–10, 12; R. 2–3.)

The co-conspirators named in the complaint are the Chadeloid Chemical Company (referred to herein as Chadeloid), a corporation which was dissolved in 1945; the manufacturers of wrinkle finishes listed in Exhibit A attached to the complaint (see R. 7–11), each of which had been during the period of the conspiracy a licensee under the wrinkle finish patent rights owned or controlled by New Wrinkle; and individuals who had acted on behalf of the defendants or the foregoing co-conspirators in carrying out the conspiracy charged in the complaint (pars. 5–7, R. 1–2).

The conspiracy had its inception in 1937. In that year and for some time earlier, K&S and Chadeloid had been engaged in litigation with respect to various patents on wrinkle finishes. Chadeloid held certain patents which it claimed were basic and K&S held other patents which it alleged provided for more economical and efficient methods of manufacture, but which Chadeloid contended were subservient to its patents. During 1937 the two companies negotiated with a view to effecting a pooling of their patents in order to eliminate competition between themselves and to set up a "licensing system" under which "prices

for the entire wrinkle finish industry would be fixed." (Pars. 14–15, R. 3.)

As a result of these negotiations, K&S and Chadeloid entered into a contract on or about November 2, 1937. The contract provided that a new corporation (defendant New Wrinkle) would be formed; that K&S and Chadeloid would each assign to New Wrinkle all of its patent rights relating to wrinkle finishes in exchange for common and preferred stock of New Wrinkle; that New Wrinkle would grant to K&S, Chadeloid and other manufacturers of wrinkle finishes non-exclusive licenses under the patents previously held by K&S and Chadeloid; and that New Wrinkle would fix minimum prices at which all licensed manufacturers might sell. A list of the principal manufacturers of wrinkle finishes was attached to the contract,[2] and it was expressly agreed that the price schedules to be prescribed by New Wrinkle would not be made effective until the Sherwin-Williams Company and eleven others of the listed manufacturers had agreed to follow the prescribed minimum prices. (Par. 16, R. 3–4.)

Following incorporation of New Wrinkle and transfer to it of the patent rights of K&S and Chadeloid relating to wrinkle finishes, New Wrinkle issued 51% of its common stock and 150 shares of preferred to K&S and 49% of its common stock and 400 shares of preferred to

[2] This list was attached to and made a part of the complaint as Exhibit B (R. 4, 11).

Chadeloid. Thereupon these companies and certain of the companies named as co-conspirators worked together to induce "the other companies in the industry" to accept patent licenses from New Wrinkle in order that competitive practices which they deemed undesirable might be eliminated. Prospective licensees were advised that other prospective licensees were being consulted "in order to establish minimum prices throughout the industry." (Pars. 17–18, R. 4.)

Representatives of K&S, Chadeloid and certain of the co-conspirators held meetings at which the terms of the licenses to be granted by New Wrinkle were agreed upon, and prices, terms, and conditions of sale were discussed. Certain licenses between New Wrinkle and manufacturers of wrinkle finishes were executed, but, as provided in the contract of November 2, 1937, price schedules were not put into effect until the Sherwin-Williams Company and eleven of the other companies listed in that contract had agreed to accept licenses. By May 7, 1938, the required number of manufacturers had signed license agreements, and the price schedules were made effective. (Par. 19, R. 4.)

From time to time after May 7, 1938, other companies, knowing that concerted action was contemplated and required in order to carry out defendants' conspiracy, entered into substantially identical license agreements with New Wrinkle

(par. 21, R. 5).[3] At the time the complaint was filed more than 200 manufacturers of wrinkle-finishes held such licenses (par. 11, R. 2). The license agreements provide, among other things, that the licensor (New Wrinkle) may establish a schedule of minimum prices, discounts and selling terms, which the licensor, the licensee, and "all other" licensees shall thereafter observe in all sales of products covered by the licensed patents; that the licensor, upon giving 30 days advance notice in writing to the licensee, may establish new minimum prices, discounts and selling terms; and that the minimum prices, discounts or selling terms prescribed by New Wrinkle shall be binding upon the licensee only if they are imposed "at the same time and in the same terms" upon the licensor and "all other" licensees (R. 13).

The license agreements run for ten years, but may be extended for "further periods" upon written notice from the licensee to the licensor given two months before the expiration date (R. 12). The licensee has the right to terminate the license at any time upon three months written notice to the licensor, and the licensor may terminate the license if the licensee violates any of its provisions and fails to remedy the violation within 30 days after written notice thereof from the licensor (*ibid.*). The royalty payable by the licensee is 5¢ per gallon of wrinkle finish sold

[3] A copy of one of these licenses is attached to the complaint as Exhibit C (R. 5, 12–13).

or used by it, but if any subsequent license is granted with lower terms of royalty, such lower terms shall apply to the licensee (R. 12, 13).

New Wrinkle, with the advice and consent of its licensees, has from time to time issued schedules of minimum prices, terms and conditions of sale to be observed by its licensees, and each licensee has adhered to the minimum prices, terms and conditions of sale set forth in these schedules (par. 22, R. 5). A copy of the schedule in effect when the Government's suit was instituted is attached to and made a part of the complaint as Exhibit D (R. 5, 15–22).

The existing schedule contains numerous provisions adapted to securing rigid uniformity in the prices and terms at which members of the wrinkle-finish industry sell their product. Granting any unauthorized discount or rebate, placing stocks on consignment, or sale of other products at "special cut prices" for the purpose of influencing the sale of wrinkle finishes constitutes a violation of the price schedule and renders the license "subject to cancellation" (R. 16).[4] Prices must be "f. o. b. destination or freight allowed" (R. 19). Terms of sale must be 30 days net, with 1% discount for payment within ten days, but this discount cannot be deducted in making bids

[4] New Wrinkle undertakes to investigate promptly any violation, and requests licensees to make prompt reports of violations and to make these reports "full and complete" (R. 16).

and is allowable only if payment is actually made within ten days after shipment (*ibid.*). Maximum quantity discounts are specified, and can be granted only on purchases under written contract (R. 18). They must be based on purchases during the 12-months period following date of contract, and the licensee must have stated the discounts to the buyer when submitting his quotation (*ibid.*). The discounts can be granted only on completion of deliveries under the contract and only if the licensee has received a statement signed by the responsible official of the buyer setting forth the quantities purchased during the contract period (*ibid.*).[5]

The products to which the prescribed minimum prices apply are specified in minute detail. The schedule recites that "the intent and purpose of the price schedule and license contract is to insure that all licensees sell at not less than the minimum price established", and that prices have been established upon the basis of sale of wrinkle finishes "in their ready to use condition" (R. 16). What constitutes "ready to use" is then minutely specified as follows (*ibid.*):

> It is, therefore, established by the Licensor that 67.5% of solids by weight is fixed as the maximum solid content of all en-

[5] The schedule also provides that each time a licensee allows a quantity discount it must attach to its next royalty report a copy of the statement received from the buyer, together with information as to the number of gallons sold to him during the contract year (R. 18).

amels ready for use except those enamels containing organic reds and maroons; and 55% of solids by weight is fixed for all enamels containing organic reds and maroons.

Supplier shall make the following determination at 60° F.: if Wrinkle Finish requires more than 10% reduction at this temperature for normal spray gun application it shall be regarded as a "concentrated material" and not "a ready for use" material and the minimum price of such "concentrated material" shall be One ($1.00) Dollar per gallon more than the established schedule of prices.

The schedule establishes minimum prices for five classifications of wrinkle finishes (R. 19). One of the classifications, "Wrinkle Finish Organics," is defined as meaning "red and maroons other than those made with oxides exclusively," to which is added: "*Any* percentage of organics in a formulation brings it under the classification" (R. 17). As to the classification "Wrinkle Finish Clear," the lowest priced product, it is provided that if it is sold under circumstances charging the licensee with knowledge that the customer intends to convert it into colored wrinkle finish, it must be sold at the minimum price prescribed for wrinkle finish "of the color and quantity in question" (R. 19). And wrinkle finish may be sold in concentrated form "only at minimum price per gallon on the number of

gallons of the kind or color of wrinkle finish" which the customer can normally produce by adding to the concentrate (*ibid.*).

The allegations with respect to interstate commerce are summarized in Point IV, *infra*, pp. 38–39.

SPECIFICATION OF ERRORS TO BE URGED

The district court erred—

1. In granting defendants' motions to dismiss the complaint.

2. In finding that defendants' motions to dismiss were well taken and should be sustained.

3. In entering judgments dismissing the complaint.

SUMMARY OF ARGUMENT

I

This case falls squarely within the established rule that a patentee who conspires with others to fix and stabilize prices and to eliminate price competition on an industry-wide basis through the medium of patent licensing agreements violates the Sherman Act and is not within any immunity therefrom given by patent law. *Standard Sanitary Mfg. Co.* v. *United States*, 226 U. S. 20; *United States* v. *U. S. Gypsum Co.*, 333 U. S. 364, 340 U. S. 76. In this case there is no problem of drawing the line between such illegal conspiracy and exercise by a patentee of monopoly rights of his patent as given recognition

in *United States* v. *General Electric Co.*, 272 U. S. 476, namely, granting a patent license with price restrictions provided such restrictions are normally and reasonably adapted to secure pecuniary reward for the exclusive right of manufacture, use and sale vested in the patentee by patent law. Here price fixing and trade-restraining agreements incident thereto were the core, the objective, and the effect of appellees' conspiracy. Indeed, establishment of price uniformity was explicitly incorporated in the patent licensing agreements, and in this respect the price-fixing character of the conspiracy was more open and avowed than in *Gypsum*. In addition, the conspiracy involved, as in *Gypsum*, maintenance of rigid and meticulous control over prices and terms of sale.

II

The fact that in this case price limitation is incorporated in license agreements made by a patentee who did not make or sell the patented product makes the doctrine of the *General Electric* case inapplicable. Price limitation was there sanctioned only to the extent that it is a normal and reasonable means of securing to the patentee royalty income from licensees without impairing his ability to secure the profit obtainable from selling the patented product himself at such prices as he chooses to charge. But when a patentee who merely grants licenses to others provides for establishing a uniform price for all

licensees, the patentee then purveys, in addition to patent production, a purported right to sell the product at controlled and fixed prices. Patents confer upon their holders no privilege to secure as a reward for the limited monopoly of the patent the value which attaches to sale of a product free from price competition. *United States* v. *U. S. Gypsum Co.*, 333 U. S. 364, 400; *United States* v. *Masonite Corp.*, 316 U. S. 265, 281, 282; *United States* v. *Vehicular Parking, Ltd.*, 54 F. Supp. 828, 838 (D. Del.).

III

United States v. *Line Material Co.*, 333 U. S. 287, held that patent law does not permit two patent owners to combine the monopolies of their individual patents for the purpose of fixing prices on products embodying their respective patents. In *Line Material* separately owned patents were pooled for this purpose by cross-licensing. In the present case such pooling of separately owned patents was effected by assigning the patents to a corporation created and controlled by the patentees. We submit that the principles of decision in the *Line Material* case are equally applicable in this situation. Moreover, here, but not in *Line Material*, the agreement under which the patentees combined their patents expressly provided for price fixing under the combined patents.

IV.

What is condemned by Section 1 of the Sherman Act is conspiring to restrain interstate commerce. Participation in such a conspiracy is therefore a violation of the section irrespective of whether the conspiring party is engaged in the interstate trade subjected to restraint or in any interstate trade. Countless decisions of this Court have so applied the Act and in the recent case of *United States* v. *Women's Sportswear Association*, 336 U. S. 460, 464, the Court expressly ruled upon this point. There is therefore no merit in New Wrinkle's contention that, because it was not engaged in interstate commerce, it was not subject to the prohibitions of the Act.

On the facts now standing admitted, it is beyond question that New Wrinkle was party to a conspiracy to fix prices on goods sold and shipped in interstate commerce. There is also no doubt that the Government's appeal challenged both dismissal of the indictment as to New Wrinkle and the legal ruling or rulings made by the district court when it found, as it cryptically stated, that New Wrinkle's motion to dismiss was "well taken." The Government in its appeal assigned such ruling or rulings as error.

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ARGUMENT

I

APPELLEES' CONSPIRACY TO FIX UNIFORM MINIMUM PRICES AND ELIMINATE PRICE COMPETITION THROUGHOUT AN ENTIRE INDUSTRY, THROUGH THE MEDIUM OF PATENT LICENSING AGREEMENTS, VIOLATES SECTION 1 OF THE SHERMAN ACT

The general principles governing the relationship between rights given by patent law and conduct forbidden by the Sherman Act are well settled. The exclusive privileges conferred by the patent grant are not deemed to involve restraint or monopolization of trade of a kind prohibited by the Sherman Act. *United States* v. *Line Material Co.*, 333 U. S. 287, 309, 310. But when the acts of a patentee are not confined to exercise of the exclusory rights vested in him by the patent grant, his conduct is governed by all prohibitions of general law, including those of the Sherman Act. Patent law gives the patentee no general right to combine with others to fix prices or otherwise to eliminate competition, and any combination of this kind, unless within the four corners of the patent grant, violates the Sherman Act. *United States* v. *Masonite Corp.*, 316 U. S. 265, 277; *United States* v. *U. S. Gypsum Co.*, 333 U. S. 364, 400, 401.

This Court has held that when a patentee himself makes and sells a product covered by his patent and licenses another to make and sell,

with the requirement that he sell at not less than the price at which the patentee sells, this restriction on the licensee's sales price comes within the implied terms of the patent grant. *United States* v. *General Electric Co.*, 272 U. S. 476.[6] The ground of decision was that this limitation is "normally and reasonably adapted to secure pecuniary reward for the patentee's monopoly," in that it enables the patentee to obtain as a reward the return coming from multiple exploitation of the exclusive rights conferred by his patent, without impairing his opportunity to obtain the reward which comes from selling the patented product himself at whatever price he thinks will bring the greatest return. 272 U. S. 476, 489–490.

But a patentee who combines or conspires with others to restrain or monopolize trade contrary to the general commands of the Sherman Act gains no immunity therefrom by reason of the fact that the objectives of the conspiracy are to be achieved through the medium of patent licensing agreements couched in terms of an exercise of patent privilege. This was the unanimous holding of

[6] In *United States* v. *Line Material Co.*, 333 U. S. 287, the district court had rested its decision on the *General Electric* case and this Court was equally divided on the question of overruling that case. A majority of the Court held, however, that the *General Electric* doctrine did not permit two patent owners, pursuant to cross licenses, to combine "to fix prices on articles covered by the respective patents" (333 U. S. at p. 312).

this Court both before and after the *General Electric* decision. *Standard Sanitary Mfg. Co.* v. *United States*, 226 U. S. 20; *United States* v. *U. S. Gypsum Co.*, 333 U. S. 364; *United States* v. *U. S. Gypsum Co.*, 340 U. S. 76.

The defendants in the *Gypsum* case had entered into patent licensing agreements providing for fixing uniform minimum sales prices, and the agreements had been made with knowledge that such price fixing was an objective of the agreements. In the first appeal the Court held that a showing that all former competitors in an industry had acted in concert to organize the industry and stabilize prices through the medium of patent licenses was sufficient to establish a violation of the Sherman Act. 333 U. S., at p. 401. The Court also held that when competition was thus suppressed, the returns thereby obtained by the patentee were not the reasonable and normal rewards of his patent monopoly contemplated and protected by patent law (*ibid*).

On the second appeal the Court, in reaffirming its prior basic rulings, held that "price-fixing licenses made in knowing concert by standardized price requirements violated the Sherman Act by their very existence." 340 U. S. 76, 86. The Court further held that, since these facts establish violation of the statute, their force is not overcome by proof that the license agreements had been made individually, and to achieve legitimate patent ends (*id.*, pp. 86–87).

Where the issue of Sherman Act violation comes before the Court after trial, there may at times be difficulty in determining whether the making of a series of patent license agreements with minimum price restrictions constitutes a conspiracy in restraint of trade which transcends mere exercise of the patentee's patent privilege. Cf. *United States* v. *Line Material Co.*, 333 U. S. 287. The present case, however, presents no problem of drawing the line between licit and illicit conduct. On the facts standing admitted, appellees' violation of the Sherman Act is clear. They are parties to a conspiracy having as its purpose the fixing of identical minimum prices and terms of sale on substantially all wrinkle finishes sold in the United States and the elimination of competition in the sale of such finishes (pars. 12, 13, 23; R. 3, 5). It was a part of the conspiracy that two patentees would pool their patents "in order to * * * set up a licensing system under which prices for the entire wrinkle finish industry would be fixed" (par. 15, R. 3). It was further a part of the conspiracy that a new corporation (appellee New Wrinkle) would be formed, that the wrinkle finish patents would be assigned to it, that it would grant licenses under these patents to the various manufacturers of wrinkle finishes, and that "minimum prices at which all licensed manufacturers might sell would be fixed by New Wrinkle" (par. 16, R. 3-4).

Price fixing is the core of the conspiracy alleged in the complaint. Indeed, charges of such a conspiracy could hardly be framed more sharply and starkly. The conspiracy, moreover, had the very elements which, in the *Gypsum* decisions, were held to be determinative of illegality. And if the facts to which we have referred were deemed not in themselves conclusive, the additional facts set forth in the complaint and presently admitted would require the conclusion that there was unlawful combination to establish and maintain industry-wide price control, not the narrowly limited type of price-fixing agreement permissible under patent law. We briefly review further admitted facts pertinent to the question of the legality of appellees' conspiracy.

The price fixing which the conspiracy was designed to bring about was not to be set in motion until 12 of the 18 "principal" producers of wrinkle finishes had signed license agreements and agreed to follow the minimum prices prescribed by New Wrinkle (par. 16, R. 4; Ex. B, R. 11).[7] This aspect of the conspiracy was carried out, and price fixing was not put into effect until 12 of the designated leaders of the industry had signed license agreements authorizing New Wrinkle to establish minimum prices and terms of sale for wrinkle finishes (pars. 19–20, R. 4–5). Prospective licensees were advised that they and

[7] One of the 12 had to be the Sherwin Williams Company (par. 16, R. 4).

others were being approached "in order to establish minimum prices throughout the industry" (par. 18, R. 4).

Approximately 200 manufacturers, representing substantially the entire domestic production of wrinkle finishes, have entered into license agreements with New Wrinkle (pars. 11–12, R. 2–3). These agreements, all of which are substantially identical, provide that New Wrinkle may prescribe minimum prices, discounts and selling terms for products covered by the licensed patents (pars. 20–21, R. 5). New Wrinkle, with the consent and advice of its licensees, has in fact prescribed such minimum prices and terms, and each licensee has adhered thereto (par. 22, R. 5). The conspiracy has resulted in the fixing and maintenance of identical and unreasonably high minimum prices, discounts, and selling terms and conditions, and in the elimination of competition, for substantially all wrinkle finishes sold in the United States (par. 23, R. 5).

The license agreements provide, specifically and somewhat redundantly, that the minimum prices and terms of sale established by New Wrinkle shall be identical for all licensees. The agreement reserves to New Wrinkle the "right" to establish such prices and terms, but only if they are also applicable to "all other Licensees" and to

New Wrinkle itself[8] (Exhibit C, R. 13). The agreement further provides (*ibid.*):

> No Schedule of Minimum Prices, Discounts and Selling Terms nor any modification or amendment or suspension thereof shall be binding upon Licensee unless at the same time and in the same terms imposed upon Licensor and all other Licensees.

While there is no doubt that the defendants in *Gypsum* had agreed and conspired to establish uniform minimum prices, the license agreements themselves did not, as here, explicitly provide for uniform minimum prices.[9] Accordingly, in the case now before the Court agreement on price uniformity is more firmly and blatantly incorporated into the license agreements than in the agreements involved in the *Gypsum* decisions. Furthermore, the Gypsum agreements permitted immediate and unheralded price changes, since a licensee was required to observe a new minimum

[8] New Wrinkle has never undertaken to make or sell wrinkle finishes (par. 11, R. 2), but if it had done so the minimum prices and terms which it had prescribed for licensees would have been binding on it.

[9] United States Gypsum Company's license agreements provided merely that the licensor may fix the licensee's minimum sales price, and that said minimum price "shall not be more than that price at which Licensor determines to sell" (333 U. S. at pp. 405–407). The licensor therefore could, without departing from the provisions of the license agreements, fix lower minimum prices for a particular licensee than those fixed for other licensees (and lower than its own sales price).

price after receipt of "written or telegraphic notice" of the change (see 333 U. S., at pp. 406–407). The provision in the New Wrinkle license agreements that no price change can go into effect until after 30 days' notice in writing to the licensee (Exhibit C, R. 13) tends to promote advance understanding and agreement upon price changes.

In the present case, just as in *Gypsum*, rigid and meticulous control over prices and terms of sale has been maintained. New Wrinkle's current edition of "License Rulings" (par. 22, R. 5, Ex. D., R. 15) states (R. 16):

> The minimum price schedule and the contract carefully specify that the intent and purpose of the price schedule and license contract is to insure that all licensees sell at not less than the minimum price established * * *.

Sales f. o. b. mill, placing stocks on consignment, and sale of other products at "special cut prices" for the purpose of influencing sale of wrinkle finishes are prohibited (R. 16, 18). The number of days credit to be given licensees' customers, the discount for early payment, and the circumstances under which the discount may be allowed are prescribed (R. 18). There are detailed provisions, including the furnishing of supporting data, regulating quantity discounts (*ibid.*). On sales of "concentrated material," licensees are required to charge one dollar per gallon more

than the established price, and such material is defined in terms of the ingredients of the product, which licensees must determine by a prescribed test (R. 16). On sale of uncolored finish, which carries the lowest prices, the licensee, if chargeable with knowledge that his customer intends to convert this product into a colored finish, must charge the price prescribed for finish of the color in question (*ibid.*). As to further details of the control exercised over prices and terms of sale, see *supra*, pp. 9–12.

The facts which have been set forth demonstrate, we believe, that appellees' conspiracy comprises the elements held to be determinative of illegality in the *Gypsum* decisions, and that the case is directly governed by these decisions.

K&S in its motion to dismiss the appeal contended that no violation of the Sherman Act was shown as to it since the complaint does not allege that K&S continued to own the New Wrinkle stock which it acquired upon the organization of that corporation (R. 25–26). Obviously K&S's participation in the conspiracy was not dependent upon either its original acquisition or its continued ownership of stock of New Wrinkle. The complaint charges a continuing conspiracy to which both K&S and New Wrinkle were parties (par. 13, R. 3) and that one of the elements of the conspiracy at its inception was organization of New Wrinkle by K&S and its co-conspirator, Chadeloid, and New Wrinkle's subsequent par-

ticipation in the conspiracy (par. 16, R. 3–4). The fact that, pursuant to the conspiracy, K&S and Chadeloid exchanged their patents for stock of New Wrinkle, instead of exchanging them for money or other consideration, is irrelevant to the conspiracy set forth. Continued ownership of New Wrinkle's stock by K&S is equally irrelevant.[10]

II

ASIDE FROM OTHER CONSIDERATIONS, APPELLEES' CONSPIRACY VIOLATES THE SHERMAN ACT BECAUSE NEW WRINKLE DID NOT MAKE OR SELL THE PRODUCT COVERED BY ITS PATENTS AND THEREFORE WAS NOT WITHIN ITS PATENT MONOPOLY WHEN IT PROVIDED IN ITS LICENSE AGREEMENTS FOR FIXING UNIFORM MINIMUM PRICES AND TERMS OF SALE

A patentee, having the exclusive right to make, use and vend his patented product, may reserve the whole field of manufacture and sale to himself. He may, if he chooses, engage in manufacture and sale, but also license others to make and sell. The *General Electric* case held that, in this situation, the patentee may forbid his licensee to undercut the patentee's own price. The

[10] The fact that K&S and Chadeloid received the stock of New Wrinkle in exchange for their patents is relevant to point III, *infra*, pp. 29–35, in that it shows the pooling of the patents of separate owners through the medium of a controlled corporation. But since the price control achieved through such pooling of patents was thereafter continued by agreement, it is immaterial in this connection whether those who pooled their patents for the purpose of fixing prices continued in stock control of New Wrinkle.

grounds of decision were that patent law permits a patentee to obtain as a reward for his invention both royalty income from licensing others and profits derived from his own sales, and that a license requirement that the licensee maintain the prices at which the patentee sells is a normal and reasonable means of assuring that receipt of income from licensing does not interfere with the full profit possibilities of the patentee's own sales of the patented product. The Court put the matter as follows (272 U. S. 476, 490):

> One of the valuable elements of the exclusive right of a patentee is to acquire profit by the price at which the article is sold. The higher the price, the greater the profit, unless it is prohibitory. When the patentee licenses another to make and vend, and retains the right to continue to make and vend on his own account, the price at which his licensee will sell will necessarily affect the price at which he can sell his own patented goods. It would seem entirely reasonable that he should say to the licensee, "Yes, you may make and sell articles under my patent, but not so as to destroy the profit that I wish to obtain by making them and selling them myself."

But when a patentee chooses as the source of his reward solely the royalties obtainable from granting patent licenses to others, a license provision that the patentee may fix minimum prices uniform for all licensees bears no relation to preservation of the profit possibilities of the

patentee's own sales of the patented product.[11] Granting of license agreements providing for such price fixing is purveying, in addition to patent protection, the opportunity to market the patented product at fixed and maintained prices. The reward of the patentee from royalty payments then represents both the value to the licensee of patent protection and the value to him of sale of the product free from price competition. Patents confer upon their holders no such privilege "to monopolize an industry through price control" (*United States* v. *U. S. Gypsum Co.*, 333 U. S. 364, 400), and under such price-fixing licenses the reward to the patentee would come in part, and in many instances in main part, "not from any preference of the public for the patented product, but from the preference of the [licensee] competitors for a mutual arrangement for price-fixing" (*United States* v. *Masonite Corp.*, 316 U. S. 265, 281). Thus to purvey price-fixing licenses is remote from price restriction on a particular licensee or a group of licensees as a means of preventing impairment of the patentee's opportunity to secure reward for his invention from his own sales of the patented product, as upheld in the *General Electric* case.

Since New Wrinkle did not make or sell the patent product (par. 11, R. 2), under the prin-

[11] In this case the amount of New Wrinkle's royalty income bears no relation to the sales price of its licenses. The royalty payable is the flat rate of 5¢ per gallon (R. 12).

ciples set forth above New Wrinkle was not within its patent monopoly when it provided in its license agreements for fixing minimum prices and terms of sale uniform for all its licensees. And the price-fixing conspiracy to which it was a party plainly violated the Sherman Act if the price fixing was not within the patentee's monopoly.

In *United States* v. *Vehicular Parking, Ltd.*, 54 F. Supp. 828 (D. Del.), a corporation which had acquired various patents on parking meters did not make or sell such meters but entered into substantially similar license agreements with concerns, representing from 95% to 98% of the industry, providing for fixing licensees' minimum prices and certain terms and conditions of sale. The facts were held to establish a conspiracy to restrain and monopolize interstate commerce in violation of Sections 1 and 2 of the Sherman Act, and the *General Electric* case was held not to apply where the patentee was a mere patent holding company. The court said (p. 838) that the decision in that case was "predicated upon the patentee making and vending the patented device," and said further (*ibid.*):

> There is nothing in that case which indicates that the patentee can agree with group-licensees to fix the price at which all may sell. * * * The price fixing, then, is for the benefit of the licensees—not to protect Vehicular's [the patentee's] sales of meters because Vehicular is not engaged in manufacturing and sale.

III.

ASIDE FROM OTHER CONSIDERATIONS, APPELLEES' CONSPIRACY VIOLATES THE SHERMAN ACT BECAUSE THE CONSPIRACY INVOLVED COMBINING THE PATENTS OF TWO OWNERS FOR THE PURPOSE OF FIXING PRICES

The conspiracy alleged in the complaint began with, and was the outcome of, negotiations between K&S and Chadeloid to effect a pooling of their patents in order to "set up a licensing system under which prices for the entire wrinkle finish industry would be fixed" (par. 15, R. 3). As a result of the negotiations, the two patent owners entered into a contract which provided for organizing New Wrinkle, assigning their patents to it, and the granting by it of price-fixing licenses under these patents (par. 16, R. 3–4). The purpose, as well as the effect, of the conspiracy thus formed was to fix identical minimum prices for substantially all wrinkle finishes manufactured and sold in the United States (par. 23, R. 5).

We submit that a combination thus to use the patents of two patent owners for the purpose of price fixing is beyond the scope of the patent monopoly. The monopoly does not expressly include the right to fix the price at which the patentee's licensee may sell the product manufactured under the patent. *United States* v. *Line Material Co.*, 333 U. S. 287, 311. It has nevertheless been held that this right is impliedly conferred under circumstances in which exercise

of such a right is "normally and reasonably adapted to secure pecuniary reward for the patentee's monopoly." *United States* v. *General Electric Co.*, 272 U. S. 476, 490. However, the patentee's right to fix prices is limited to securing "a reward for his invention"; he goes beyond this when the effect of price-fixing license provisions is to "enhance the value of his own trade position by eliminating or impairing competition." *United States* v. *Masonite Corp.*, 316 U. S. 265, 282.

In *United States* v. *Line Material Co.*, 333 U. S. 287, the holder of a dominant patent and the holder of a subservient patent entered into cross-licensing agreements which gave to Line, the holder of the subservient patent, the exclusive right to license the dominant patent. Line thereupon granted licenses under both patents, and provided therein that the licensee maintain Line's sales prices on devices which embodied Line's patent. The Court pointed out (p. 307) that although in terms Line's price fixing was limited to its own patent, the price fixing was also effective as to devices embodying the necessary dominant patent. The Court accepted the continued authority of the *General Electric* case insofar as that case had held that a single patentee may restrict his licensee's sales price. But the Court held (p. 311) that the patentee's monopoly, as given recognition in the *General Electric* case, does not sanction a merger of the price-fixing powers of two

patentees, and does not permit "separate owners of separate patents by cross-licenses or other arrangements to fix the prices to be charged by them and their licensees for their respective products." The Court pointed out (p. 315) that what was unlawful was not the cross-licensing itself but use of the control thereby given to fix prices.

Since the price fixing in which the defendants in *Line Material* had engaged was in clear violation of the Sherman Act, apart from patent or other statutory exemption, the defendants' knowing joinder in like price-fixing licenses brought their combination under the prohibitions of the Sherman Act when their claim of patent privilege failed.

In the present case the circumstances under which separate owners joined their patents for price-fixing purposes point more strongly to action beyond the scope of the patent monopoly than in the *Line Material* case. The dissenting opinion in that case noted (333 U. S. 326) that the cross-licensing—the means by which the patents of separate owners were used in combination—did not either require or provide for price fixing. Here, in contrast, the agreement for uniting the patents of separate owners provided for using the combined patents to set up a price-fixing licensing system. Thus a major factual element which led to the cleavage in the Court as to the proper result in the *Line Material* case is lacking here.

Under the *Line Material* decision, the Sherman Act would have been violated if K&S and Chadeloid had cross-licensed each other and one of them had, pursuant to the authority thereby conferred, granted uniform price-fixing licenses under both patents, accepted by licensees with knowledge of like acceptance by others. The same fixing of prices through combining separately owned patents was achieved when K&S and Chadeloid organized New Wrinkle and assigned their patents to it for the purpose of setting up a price-fixing licensing system. We submit that what they were not authorized to do directly they were not authorized to do through a corporate agent created by them to accomplish the forbidden end.

In *Standard Sanitary Mfg. Co.* v. *United States*, 226 U. S. 20, this Court unanimously condemned price limitations effected through assignment of patents to a third person to act as licensor. There patents held by Standard and two of its competitors were assigned by them to the secretary of a trade association. He, in turn, granted licenses under the patents and fixed the prices at which licensees might sell. The Court, in holding that these arrangements violated the Sherman Act, said (p. 49) that the "element of the patent in the case at bar cannot confer immunity * * *, for the reasons we have

stated." Earlier in its opinion the Court said (p. 48):

> The agreements clearly, therefore, transcended what was necessary to protect the use of the patent or the monopoly which the law conferred upon it. They passed to the purpose and accomplished a restraint of trade condemned by the Sherman law.

The *Line Material* case applied the general principle of the *Standard Sanitary* case where separate patent owners had combined their patents through cross licensing, and had thus achieved price fixing. We submit that the method by which such combination is achieved—whether by "cross-licenses or other arrangements"—is immaterial. See *Line Material* case, p. 311. The Sherman Act "is aimed at substance rather than form." *United States* v. *Yellow Cab Co.*, 332 U. S. 218, 227. In situations where, as here, there has been a strong public interest to be protected, this Court has consistently looked to the realities of the transaction."[11]

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[11] The Court has refused to find a valid corporate reorganization for tax purposes where, although the transaction met the literal requirements of the statute, it served no business purpose. *Gregory* v. *Helvering*, 293 U. S. 465; cf. *Bazley* v. *Commissioner*, 331 U. S. 737. It has disregarded the existence of a family partnership between husband and wife, valid under state law, and taxed the entire income to the husband, when the partnership income in fact was earned by the husband. *Commissioner* v. *Tower*, 327 U. S. 280; cf. *Commissioner* v. *Culbertson*, 337 U. S. 733. The corporate

In *United States* v. *Masonite Corp.*, 316 U. S. 265, Masonite, holding patents on hardboard, manufactured and sold its patented product, and also entered into patent licensing agreements with companies engaged in the sale of competing products. The agreements authorized the licensees to sell Masonite's patented product as *del credere* agents, at not less than the prices at which Masonite sold. This Court held that when Masonite thus used the selling organizations of its competitors for marketing its patented product, the exclusive right to "vend" given by patent law was exhausted when Masonite put the product in the hands of its "agents," and that the scope of the patentee's right to vend "cannot be determined by reference to the private law of sales alone." 316 U. S. 265, 278–280. The Court said (p. 280):

> Since patents are privileges restrictive of a free economy, the rights which Congress has attached to them must be strictly construed so as not to derogate from the general law beyond the necessary requirements of the patent statute. *United States* v. *Univis Lens Co., Inc., supra.* So far as

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entity concept has been disregarded when necessary to give minority stockholders redress against injury to their interests by a majority stockholder. *Taylor* v. *Standard Gas & Electric Co.*, 306 U. S. 307, 322.

> the Sherman Act is concerned, the result must turn not on the skill with which counsel has manipulated the concepts of "sale" and "agency" but on the significance of the business practices in terms of restraint of trade.

To permit combining separately owned patents for price-fixing purposes through the medium of a corporation created and controlled by the patentees, when like combination through the medium of cross-licensing stands forbidden, would not only be highly anomalous; it would leave open a wide loophole for the utilization of patents to bring an industry under price control.

In *United States* v. *General Instrument Corp.*, 87 F. Supp. 157 (D. N. J.), several patentees organized a new corporation and assigned their patents to it with power to grant licenses thereunder. For a period of time the corporation issued licenses fixing licensees' minimum sales prices. The court (p. 193) rejected the defense that this price fixing was permissible under the *General Electric* case, and held that the *Line Material* case was controlling. The court said that the fact that the licensor was the patent holding company, rather than one of the patentees, "is a mere matter of form and does not alter the substance of the arrangement."

IV

NEW WRINKLE VIOLATED THE SHERMAN ACT BY BEING A PARTY TO A CONSPIRACY TO RESTRAIN INTERSTATE COMMERCE IN WRINKLE FINISHES, IRRESPECTIVE OF WHETHER IT WAS ITSELF ENGAGED IN INTERSTATE COMMERCE

Appellee New Wrinkle argues that since it does not manufacture or sell any of the wrinkle finishes it is not in interstate commerce, and therefore cannot be guilty of violating the Sherman Act.

It is elementary that what Section 1 of the Sherman Act condemns is the act of conspiring to impose unlawful restraints on interstate or foreign commerce. *United States* v. *Socony-Vacuum Oil Co.*, 310 U. S. 150, 225. A party to such a conspiracy therefore violates the Act whether or not his own interstate trade is restrained and whether or not he is engaged in any interstate trade. From the outset the Act has been applied to those who were parties to the forbidden conspiracies though they were not engaged in the commerce subjected to restraint. This Court has so applied the Act to trade associations in scores of cases, beginning with the cases of *United States* v. *Trans-Missouri Freight Assn.*, 166 U. S. 290; *United States* v. *Joint Traffic Assn.*, 171 U. S. 505. It was so applied at an early date to a holding company formed to bring two competing railroads under single control (*Northern Securities Co.*, v. *United States*,

193 U. S. 197) and to labor unions and their members (*Loewe* v. *Lawlor*, 208 U. S. 274). And the Court recently rejected a similar contention in *United States* v. *Women's Sportswear Association*, 336 U. S. 460, 464, wherein it said:

> The trial court appears to have dismissed the case chiefly on the ground that the accused Association and its members were not themselves engaged in interstate commerce. This may or may not be the nature of their operation considered alone, but it does not matter. Restraints, to be effective, do not have to be applied all along the line of movement of interstate commerce. The source of the restraint may be intrastate, as the making of a contract or combination usually is; the application of the restraint may be intrastate, as it often is; but neither matters if the necessary effect is to stifle or restrain commerce among the states. If it is interstate commerce that feels the pinch, it does not matter how local the operation which applies the squeeze.

Similarly unsound is New Wrinkle's contention that the mere granting of patent licenses does not subject it to the Sherman Act. *Standard Oil Company* v. *United States*, 283 U. S. 163. This Court there stated (pp. 168–9):

> The defendants contend that the agreements assailed relate solely to the issuance of licenses under their respective patents; that the granting of such licenses, like the

> writing of insurance, *New York Life Ins. Co.* v. *Deer Lodge County,* 231 U. S. 495, is not interstate commerce; and that the Sherman Act is therefore inapplicable. This contention is unsound. Any agreement between competitors may be illegal if part of a larger plan to control interstate markets. * * * Moreover, while manufacture is not interstate commerce, agreements concerning it which tend to limit the supply or to fix the price of goods entering into interstate commerce, or which have been executed for that purpose, are within the prohibitions of the Act.

The complaint herein charges generally that appellees have been and are engaged in a combination and conspiracy in restraint of trade and commerce among the several states (par. 13, R. 3). In amplification, it is alleged that although New Wrinkle is not engaged in commercial manufacture and sale, it owns or controls patents which it licenses to manufacturers located "throughout the various states" (pars. 11–12, R. 2–3), and that a "substantial portion of the wrinkle finishes made by licensees is sold to purchasers in states other than those in which the finishes are manufactured and to purchasers in the Dominion of Canada, and is shipped from one state to another, and from various states of the United States to various locations in the Dominion of Canada in the ordinary course of business" (par. 12, R. 3). The complaint describes the manner

in which the sales prices of the manufacturer-licensees were fixed (pars. 19–22, R. 4–5), and then states that the conspiracy had the intended effect "of fixing and maintaining identical and unreasonably high and arbitrary minimum prices, discounts and selling conditions and terms for substantially all wrinkle finishes manufactured and sold in the United States, and of eliminating competition between the defendants and co-conspirators in the sale of such finishes" (par. 23, R. 5).

These allegations that prices are fixed on substantially all sales in the United States, that a substantial portion of the sales is to purchasers in other states (par. 12, R. 3), and that New Wrinkle was a party to the price-fixing conspiracy (par. 13, R. 3), clearly charge a conspiracy by New Wrinkle to fix prices in interstate commerce.

Since New Wrinkle was a party to all the price-fixing contracts and, indeed, was organized in large part for the purpose of fixing prices for the industry (pars. 15–21, R. 3–5), it is obvious that, under the above allegations, it has restrained trade and commerce among the several states whether or not it was in interstate commerce itself. Accordingly, we remain of the view expressed in the Government's jurisdictional statement that New Wrinkle's contention that it is outside the prohibitions of the Act because it is

not engaged in interstate commerce appears almost frivolous.

New Wrinkle argued, in a motion to dismiss, that the Government has not appealed from the district court's adverse decision as to it. The contention was that New Wrinkle's motion to dismiss the complaint had been based upon the commerce issue and that the Government had not assigned error to the district court's decision on this point or included it within the Questions Presented in the Statement as to Jurisdiction. It is difficult to believe that the cryptic order of the district court (R. 27) could have rested on so obviously insubstantial a ground. Compare the order as to K&S (R. 28). In any event the Government's assignment of errors is sufficient to allege error in this respect. The assignments were not required to be more specific in the absence of any statement of reasons by the district court, and the point was referred to in the Government's Statement as to Jurisdiction (p. 7, n. 3). The Government's reply to New Wrinkle's motion to dismiss deals with this question fully, and it seems unnecessary to repeat that discussion here. This Court has power, of course, to review a plain error even if unassigned. Supreme Court Rule 27 (6); *United Brotherhood of Carpenters* v. *United States*, 330 U. S. 395, 412, and cases cited.

CONCLUSION

For the foregoing reasons, the judgments of the district court dismissing the complaint should be reversed.

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